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Market Tone

The USD dollar (USD) is starting the year with broad weakness, reflecting a mix of weaker data and deteriorated sentiment. The labour market is showing signs of renewed softness, weighing on consumer confidence and hinting to intensifying headwinds for the US economy. Fed policymakers are calibrating their response within the context of a complex relationship to the US administration, given judicial proceedings against Chair Powell and the nomination of the traditionally orthodox Kevin Warsh.

We have made no changes to our FX forecast, and we continue to expect broad-based weakness in the USD against all of the major developed economy currencies. The weak USD forecast extends through 2026 and into the end of our forecast horizon at the end of 2027, reflecting an outlook for relative central bank policy that includes near-term Fed easing, steady policy settings for the Fed's peers, and longer-term tightening from some of the smaller growth-sensitive central banks whose economies are more closely tied to global commodity prices.

Growth trends in the US are mixed, with ongoing challenges in housing and manufacturing balanced against resilient services. The media's breathless coverage of high profile investment in the technology sector, to support the build out of artificial intelligence, remains an important source of confidence. Financial conditions remain

Continued on next page ...

FX Forecasts

		2025a	2026f	2027f	2026f				2027f			
					Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Major Currencies												
Japan	USDJPY	157	140	130	147	145	142	140	137	135	133	130
Euro zone	EURUSD	1.17	1.22	1.24	1.18	1.18	1.22	1.22	1.23	1.23	1.24	1.24
	EURJPY	184	171	161	173	171	173	171	169	166	165	161
UK	GBPUSD	1.35	1.37	1.39	1.32	1.34	1.36	1.37	1.38	1.38	1.39	1.39
	EURGBP	0.87	0.89	0.89	0.89	0.88	0.90	0.89	0.89	0.89	0.89	0.89
Switzerland	USDCHF	0.79	0.76	0.77	0.78	0.78	0.76	0.76	0.76	0.76	0.77	0.77
	EURCHF	0.93	0.93	0.95	0.92	0.92	0.93	0.93	0.94	0.94	0.95	0.95
Americas												
Canada	USDCAD	1.37	1.33	1.30	1.38	1.35	1.34	1.33	1.32	1.32	1.30	1.30
	CADUSD	0.73	0.75	0.77	0.72	0.74	0.75	0.75	0.76	0.76	0.77	0.77
Mexico	USDMXN	18.01	18.01	18.77	17.52	17.68	17.84	18.01	18.19	18.39	18.58	18.77
	CADMXN	13.12	13.54	14.44	12.70	13.10	13.31	13.54	13.78	13.93	14.29	14.44
Brazil	USDBRL	5.47	5.50	5.50	5.33	5.40	5.45	5.50	5.50	5.50	5.50	5.50
Chile	USDCLP	901	870	870	870	870	870	870	870	870	870	870
Peru	USDPEN	3.36	3.35	3.45	3.39	3.32	3.35	3.35	3.40	3.37	3.42	3.45
Asia-Pacific												
Australia	AUDUSD	0.67	0.70	0.72	0.68	0.68	0.70	0.70	0.71	0.71	0.72	0.72
New Zealand	NZDUSD	0.58	0.64	0.66	0.60	0.62	0.64	0.64	0.65	0.65	0.66	0.66

f: forecast a: actual

CAD FX Forecasts

		Canadian Dollar Cross-Currency Trends								
FX Rate	Spot 12-Feb	26Q1f	26Q2f	26Q3f	26Q4f	27Q1f	27Q2f	27Q3f	27Q4f	
AUDCAD	0.97	0.94	0.92	0.94	0.93	0.94	0.94	0.94	0.94	
CADJPY	112	107	107	106	105	104	102	102	100	
EURCAD	1.62	1.63	1.59	1.63	1.62	1.62	1.62	1.61	1.61	
USDCAD	1.36	1.38	1.35	1.34	1.33	1.32	1.32	1.30	1.30	

Market Tone

conducive to the effective transmission of monetary policy, however there appears to be an elevated sensitivity to any sign of deterioration. The presidential cycle is an added consideration for investors, given that mid-term years are historically challenging for equity markets.

Scotiabank's Fed forecast continues to anticipate 75bps of easing in 2026, with 50bps in Q1 and a final 25bp cut in Q2, delivering a terminal policy rate of 3.00% for this easing cycle. The rate is expected to remain unchanged at 3.00% through the end of our forecast horizon (Q4 2027). Softened data and prospective leadership changes at the Fed are tilting the balance of risk toward greater easing, not less. Chair Powell's presumed replacement, nominee Kevin Warsh, is a former Fed governor with extensive private financial sector experience across major banks and hedge funds. His policy views lean toward a more orthodox execution of the Fed's remit, preferring conventional (interest rate) policy over unconventional (balance sheet, communication) tools that have been deployed over the past 15–20 years. A Warsh-led Fed would likely lean toward lower rates as a counterweight to balance sheet normalization and favour less communication.

Structural trends also favour medium-term USD weakness, given wide fiscal and current account deficits that are expected to broaden even further. The risks for the USD are a major—and intensifying—concern for global investors, whose increasing demand for hedging protection will only serve to add to the bearish pressure on the USD.

The theme of trade policy uncertainty has extended into 2026, generating the first round of broad-based USD weakness in mid/late-January as market participants responded to President Trump's tariff threats in response to his pursuit of Greenland. A weaker USD remains the most effective lever to support the president's trade objectives.

Upside risks to our USD forecast centre on the outlook for inflation, and the possibility of a renewed upswing, in a manner similar to that observed in the late 1970s, when a resurgence followed the initial decline from the mid-1970s peaks. Oil prices remain critical to this risk, and we remain tightly focused on geopolitical developments.

The Canadian dollar (CAD) has had a choppy start to the year, initially weakening in response to weaker oil prices and wider US-Canada spreads but ultimately recovering to end January with a push to fresh 16-month highs. The CAD's latest gains have been fundamentally driven, reflecting softened Fed expectations that have narrowed interest rate differentials in the CAD's favour. The Bank of Canada (BoC), on the other hand is decidedly neutral and highlighting the limited impact of monetary policy in managing structural challenges. A meaningful recovery in oil prices also appears to be underway, adding to the CAD's fundamental gains.

The accommodation provided by the BoC's 2025 rate cuts have delivered an important source of support for the Canadian economy, complementing the stimulus provided by the latest Federal budget. The BoC is expected to deliver 50bps of tightening in 2026, with one 25bp hike in each of the final quarters of the year. Another 25bp hike in Q1 2027 will lift the BoC's policy rate to 3.00%, fully eliminating the policy rate gap to the Fed. We have made no changes to our USDCAD forecast, targeting 1.33 for the end of 2026 and 1.30 by the end of 2027. Trade policy risks remain a major source of uncertainty to our forecast, given the renegotiation of the USMCA that is scheduled for July 1st, 2026.

The euro (EUR) traded defensively to start the year but quickly bounced back in response to sentiment-related weakness in the USD. The EUR's subsequent gains delivered a break to fresh highs reaching levels last seen in 2023. The European Central Bank (ECB) has maintained a decidedly neutral tone for several months, cautiously fading a dovish bias that had been introduced on the basis of trade policy uncertainty. Sterling (GBP) faces some near-term uncertainty related to politics and PM Starmer's ability to remain in government. The currency remains fundamentally 'cheap' however, and mixed data have forced markets to soften their expectations for easing from the Bank of England (BoE). For JPY, the outcome of the latest election has delivered a resounding mandate for PM Takaichi along with a relief rally in the yen (JPY). Market participants had been concerned about the PM's fiscal platform and hopes for central bank cooperation, and have responded positively to Takaichi's message of continuity and coalition building as she purses her goals. The risk of another Bank of Japan (BoJ) pause appears to be moderating, as market participants consider policymakers' undaunted and public expressions of their preference for continued tightening, calling for rate hikes at some point in 2026. Lower US yields and tighter US-Japan spreads should deliver fundamental support to the yen in 2026.

For Latam FX, a multitude of developments offer mixed drivers for different currencies. Slowing economic growth in the US is a negative for Mexico and the peso (MXN), however this is balanced by a broad rise in commodity prices that should deliver better terms of trade for Chile and its peso (CLP). Elections in Brazil and Chile are scheduled for October and November, respectively, and will provide considerable headline risk in the back half of 2026.

Federal Reserve and Bank of Canada Monetary Policy Outlook

FEDERAL RESERVE—FURTHER EASING AHEAD

We forecast with modest confidence three rate cuts this year down to a 3% fed funds overnight rate followed by a prolonged hold. We haven't given up on March since there is still a lot of data on jobs and inflation to sift through before then, but the odds have grown slimmer.

Inflation risk remains material, but we think the Committee will respond more to the evidence of a deteriorating job market while moving toward a more neutral stance. One reason for this is that it's often how they've behaved in the past.

A second reason is that if the job market is deteriorating, then it could be a leading sign of broader problems in the economy that would diminish capacity pressures and hence reduce inflation risk. For example, the pace of nonfarm payroll gains began ebbing and turned negative well before markets and GDP fell in late 2008.

Third is that the job market is deteriorating even after a rather illusory recent gain ([here](#)) and the drop in the unemployment rate is doubtful ([here](#)). Chart 1 shows that nonfarm payrolls excluding health care and social assistance have been weak for an extended period. Of nonfarm's 130k gain in January, 124k came through health care and social assistance (42k) that are vulnerable to expired ACA subsidies.

On the hawkish side is upside inflation risk and that has several on the FOMC worried. The US economy is still in excess demand, and supply chain cost pressures are likely to rise. Tariffs are only a subset of such pressures. It's too soon to say productivity growth may temper some of the inflation risk and the US could be in an AI-investment bubble.

Chair Powell hands over to Chair-nominee Warsh after April. Warsh will then need data to back any dovish bias to convince a majority of the 12 FOMC members that cutting is the correct way to proceed.

BANK OF CANADA—NEXT MOVE UP?

The BoC is forecast to be on a long pause at an overnight rate of 2.25% until we have 75bps of hikes over late 2026Q4 into 2027. Elevated uncertainty means there are non-zero probabilities to many rate scenarios.

Don't expect much from the BoC anytime soon. The BoC's recent communications are ambivalent toward the direction or timing of the next policy rate move because they lack confidence in assigning probabilities to different scenarios.

They describe the policy rate as remaining appropriate while evaluating developments (recap [here](#)).

Governor Macklem's recent [speech](#) reminded markets that the BoC won't just be looking at demand-side activity readings like GDP but is concerned about the supply side and hence determining whether developments are cyclical or structural in nature. The answer is important to assessing inflation risk and will take a lot of time and data to evaluate.

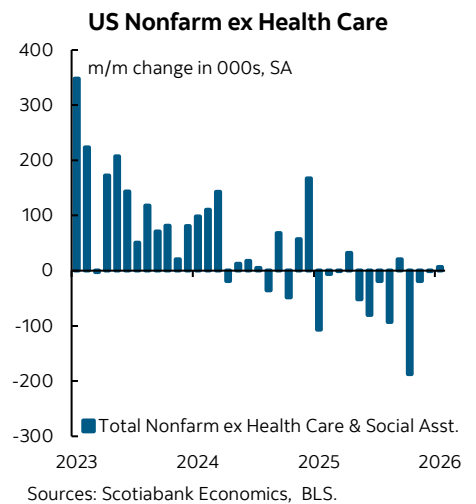
Our foundations for a future tightening bias include a starting point of a zero real policy rate at the lower bound of neutral rate estimates that offers insurance against downside risks. It's too soon to evaluate the full effects of past monetary easing.

We expect the economy to gradually gain traction through fiscal policy, distance from initial trade shocks, and an eventual release of pent-up demand for cap-ex, consumption and housing investment. Zero population growth is an exaggerated shock as it is mostly due to temps.

The most likely CUSMA scenarios are a successful negotiation or a protracted period of annual reviews. The economy can adapt to either scenario. Almost 90% of Canadian exports to the US are tariff free and CAD has depreciated 16 cents from its 2021 peak.

Spare capacity is expected to be shut over our forecast horizon while supply side constraints and rising cost pressures merit continued caution on inflation risk.

Chart 1



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North America

USD

USD Outlook Remains Negative

Current spot 1180.20



Source: Bloomberg.

USD—The USD is starting 2026 much the same way that it began 2025—on the defensive. In broad terms, the USD is also tracking the contours of price action seen in the early stages of President Trump’s first term, suggesting the defensive undertone may persist in the short run before some consolidation develops perhaps. Sentiment is broadly bearish and we remain negative on the USD outlook given our forecast for easier Fed policy in H2 (as most other major central banks remain sidelined) and the current focus on investors reducing overweight exposure to USD-denominated assets. The dollar index could fall another 4–5% in the coming months.

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USDCAD

CAD Progress Hampered by Trade Uncertainty

Current spot 1.3608



Source: Bloomberg.

USDCAD—The CAD is a little firmer so far in 2026 but it remains an underperformer relative to its core currency peers. Trade uncertainty remains a drag on the outlook and Canadian terms of trade have not fully reflected recent gains in commodity prices. Positioning and sentiment data suggest a cautiously constructive view on the CAD outlook and seasonality is typically CAD-bullish as we get deeper into the spring (especially April). In the short run, the CAD may have difficulty decoupling from risk appetite and the broader USD trend as drivers, however. Investors want—and the economy needs—clarity on what sort of trade relationship Canada will have with the US.

Scotia Forecasts

Q1-26	1.38	Q2-26	1.35	Q3-26	1.34	Q4-26	1.33
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USDMXN

MXN Supported by High Domestic Yields

Current spot 17.2025



Source: Bloomberg.

USDMXN—The MXN has appreciated significantly in recent weeks, supported by the general weakness in the USD, the relative appeal of domestic interest rates and the currency’s high liquidity. Additional factors such as still-elevated remittances and the competitive advantage provided by the USMCA have contributed to MXN strength. Looking ahead, upside risks include a favourable outcome in the USMCA review, persistent geopolitical tensions that continue to weaken the USD, and a US political scenario favourable to Republicans. Downside risks for the MXN include a negative USMCA renegotiation outcome, domestic tensions, economic or fiscal deterioration, and a sharp adjustment in the large speculative long MXN positions currently held on the Chicago derivatives market.

Scotia Forecasts

Q1-26	17.52	Q2-26	17.68	Q3-26	17.84	Q4-26	18.01
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Major Currencies

EURUSD

EUR Gains Test Major Resistance

Current spot 1.1885



Source: Bloomberg.

EURUSD—The EUR retains a bullish undertone, trading a little above our H1 2026 forecast (1.18). We expect more gains over the balance of the year as investor concerns about elevated US high-tech stocks drive further rotation toward firm European equities. Economic prospects remain muted and additional sharp gains may attract ECB attention, even though the central bank’s own research indicates that exchange rate passthrough to prices is typically limited. Lower rates remain unlikely at this stage. Technically, solid EUR gains are testing key, long-term resistance defined by the 200-month MA (1.1940). A clear and sustained extension through the mid-1.19 area would suggest more medium-term EUR gains.

Scotia Forecasts

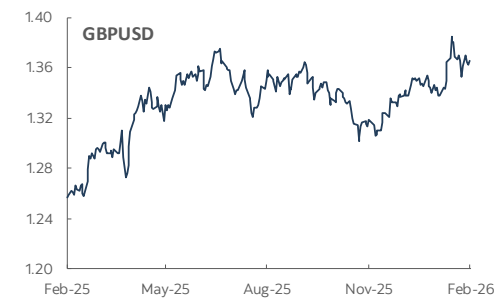
Q1-26	1.18	Q2-26	1.18	Q3-26	1.22	Q4-26	1.22
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GBPUSD

GBP Shrugs Off Fiscal, Political Concerns

Current spot 1.3643



Source: Bloomberg.

GBPUSD—The pound has performed well so far this year, despite some recent politically induced volatility. Investors were perhaps too negatively positioned on the pound in late 2025 amid concerns over the UK government’s weak fiscal policy outlook. The Chancellor’s budget late last year addressed several key concerns (some relief for struggling families, some tax increases), helping ease investor worries. Some additional monetary easing from the BoE remains a risk, however. Scotia forecasts—and swaps markets have largely priced in—a further 50bps of rate cuts over the balance of this year which may drive some GBP underperformance on the crosses.

Scotia Forecasts

Q1-26	1.32	Q2-26	1.34	Q3-26	1.36	Q4-26	1.37
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USDCHF

CHF Lifted by Haven Demand

Current spot 0.7713



Source: Bloomberg.

USDCHF—The CHF is a moderate outperformer so far in 2026 but gains are taking the currency to the highest versus the USD and EUR seen since the extreme volatility in 2015 when the SNB abandoned its EURCHF 1.20 peg. Heightened market volatility and geopolitical uncertainty in January and February helped support the recent currency gains. The strong exchange rate is prompting speculation about what, if anything, the SNB can do to counter the trend. Amid rising uncertainty around the USD outlook, few alternative havens and a policy rate at zero, the answer—for now—may be very little. That may mean the EURCHF “undershoots” our 0.92 forecast for H1 for an extended period.

Scotia Forecasts

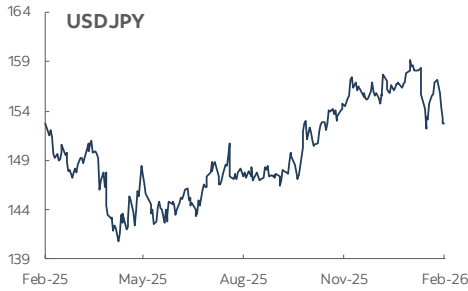
Q1-26	0.78	Q2-26	0.78	Q3-26	0.76	Q4-26	0.76
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Major Currencies (continued...)

USDJPY

JPY Underperforms Despite Supportive Yield Spreads **Current spot 152.53**



Source: Bloomberg.

USDJPY—The JPY has underperformed broadly so far in 2026. The currency’s weak undertone in January, when it traded near 160, prompted the Bank of Japan and the Fed to call around trading desks to “check prices”, signalling extreme official discomfort with price action. The JPY snapped higher in response and while no direct intervention appears to have taken place, the 160 zone is clearly an area of intensified concern for the authorities. PM Takaichi’s sweeping win in the snap election has been accompanied by soothing comments on fiscal policy which may reassure markets and allow the JPY to reconnect with narrowing, JPY-supportive US/Japan interest rate spreads and push spot back under 150.

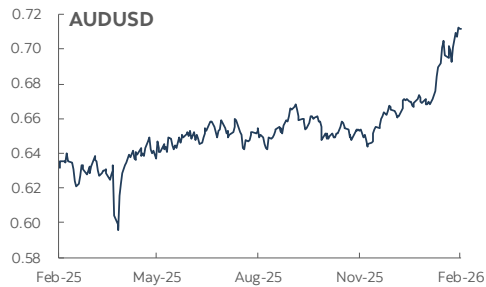
Scotia Forecasts	Q1-26	147	Q2-26	145	Q3-26	142	Q4-26	140
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Australia

AUDUSD

Solid AUD Gains May Extend Above 0.70 **Current spot 0.7104**



Source: Bloomberg.

AUDUSD—The AUD is the best-performing major currency YTD, rising more than 5% at writing. Surging industrial and precious metals backed robust AUD gains in early-2026 trading while a 25bp increase in the Reserve Bank of Australia’s policy rate (to 4.85%) provided an additional lift for the currency in February. Yields plus currency appreciation have given the AUD emerging market-like total returns (more than 10%) over the past three months, finally forcing persistently bearish positioning and sentiment to reassess prospects. Strong technical gains in the AUD in early 2026 have broken long-term bear trend resistance and indicate the potential development of a new, higher trading range above USc70 may be developing.

Scotia Forecasts	Q1-26	0.68	Q2-26	0.68	Q3-26	0.70	Q4-26	0.70
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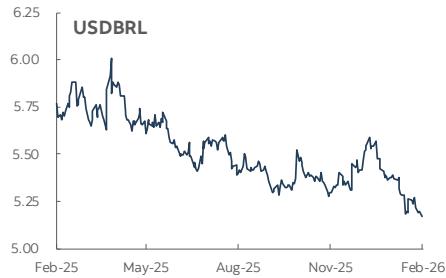
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Latin America

USDBRL

Yields, Local Politics Help Lift BRL

Current spot 5.1758



Source: Bloomberg.

USDBRL—The BRL recently gained through 5.20 per USD—its strongest since mid-2024—amid favourable domestic and carry fundamentals, shifting political expectations, and broad USD weakness. Optimism ahead of the October vote has also supported local assets. Flavio Bolsonaro’s (the former president’s son) has gained ground in surveys against incumbent Lula. Reduced BCB cut bets amid inflation persistence and firm growth have also helped the BRL. BCB expectations and moves in polls are key near-term BRL catalysts. Its latest undershoot relative to our forecasts seems overdone and prone to reversal toward ~5.40, though the improved political outlook may augur a lower end-2026 forecast than our current ~5.50 call.

Scotia Forecasts

Q1-26	5.33	Q2-26	5.40	Q3-26	5.45	Q4-26	5.50
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USDCLP

CLP Trades in Line with Fundamentals

Current spot 865.12



Source: Bloomberg.

USDCLP—The CLP has appreciated by about 9% since late 2025, supported by a 23% increase in LME copper prices and a 2% depreciation of the USD. In this context, we estimate that the political risk premium previously reflected in the currency—relative to both developed and emerging-market currencies—has largely dissipated. For now, the CLP is trading at levels more consistent with the fundamental variables that determine its long-term equilibrium value. We continue to project USDCLP at around 870 toward the end of 2026, supported primarily by strong copper prices, a favorable interest-rate differential relative to the Fed and improved GDP growth prospects that should further reinforce the peso’s strength.

Scotia Forecasts

Q1-26	870	Q2-26	870	Q3-26	870	Q4-26	870
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USDPEN

Intervention Curbs PEN Strength

Current spot 3.3540



Source: Bloomberg.

USDPEN—The sol has remained very stable, at around PEN3.35 over the past three months (since November 2025), making it the currency with the lowest volatility in the region. Appreciation pressures remain strong, given external conditions—such as high metal prices and weakness in the DXY—and the increased inflows from foreign investors into Peru due to its solid economic fundamentals. However, the BCRP has been actively intervening in both the spot and derivatives markets to curb appreciation. Intervention totals slightly more than USD3.4bn and USD4.0bn respectively so far this year. We project that the exchange rate will remain around PEN3.35 at year-end, assuming that the outcome of the presidential elections is favourable for the economic environment.

Scotia Forecasts

Q1-26	3.39	Q2-26	3.32	Q3-26	3.35	Q4-26	3.35
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Ricardo Avila, Peru

FOREIGN EXCHANGE STRATEGY

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